



2009
Annual Report

Item 1. Exact name of the issuer and the address of its principal executive offices.

The exact name of the issuer is YoCream International, Inc.

The address of the issuer's executive office is as follows:

YoCream International, Inc.
5858 NE 87th Avenue
Portland OR 97220-1312

Phone: 503-256-3754
Fax: 503-416-2495
Website: www.yocream.com

Investor Relations: Terry Lusetti
Phone: 503-256-3754
E-mail: terryl@yocream.com

Item 2. Shares outstanding.

2009 fourth fiscal quarter:

Period end date	October 31, 2009
Common Stock	
(i) Authorized	30,000,000
(ii) Issued and outstanding	2,607,898
(iii) Freely tradeable shares (estimated public float)	1,025,000
(iv) Total number of beneficial shareholders	N/A
(v) Total number of shareholders of record	116
Preferred Stock	
(i) Authorized	5,000,000
(ii) Issued and outstanding	-
(iii) Freely tradeable shares (public float)	-
(iv) Total number of beneficial shareholders	-
(v) Total number of shareholders of record	-

Item 3. Annual financial statements.

The following audited financial statements for the Company's fiscal years ended October 31, 2009 and 2008 are attached to this report and are incorporated by reference herein.

Independent Auditor's Report
Balance Sheets
Statements of Income
Statements of Cash Flows
Statements of Changes in Stockholder's Equity
Notes to Financial Statements

Item 4. Management's discussion and analysis

Forward-Looking Statements

This Management's Discussion and Analysis and other sections of this Report contain forward-looking statements within the meaning of the Securities Litigation Reform Act of 1995 that are based on current expectations, estimates and projections about the Company's business, management's beliefs, and assumptions made by management. Words such as "expects," "anticipates," "intends," "plans," "believes," "seeks," "estimates" and variations of such words and similar expressions are intended to identify such forward-looking statements. These statements are not guarantees of future performance and involve risks and uncertainties that are difficult to predict. Therefore, actual outcomes and results may differ materially from what is expressed or forecasted in such forward-looking statements due to numerous factors including changes in demand for the Company's products, product mix, level of customer acceptance of new products, changes in customer relationships and strategic alliances, changes in distribution capabilities, excess or shortage of production capacity, changes in competitive or regulatory conditions affecting the Company's products, operations, pricing or service, and other risks discussed in this Report and from time to time in the Company's other financial reports. In addition, such statements could be affected by general industry and market conditions and growth rates, and general domestic and international economic conditions. Such forward-looking statements speak only as of the date on which they are made and the Company does not undertake any obligation to update any forward-looking statement to reflect events or circumstances after the date of this Report.

Results of Operations

YoCream International, Inc. is a world leader in the frozen yogurt industry. Since 1977, YoCream has pioneered the innovation, production and marketing of frozen yogurt and fruit-based frozen desserts and beverages. The Company operates a state-of-the-art production facility in Portland, Oregon, to manufacture its "true" frozen yogurt, which contains the real yogurt that is fermented and cultured on site daily.

YoCream's products are characterized by great flavor and significant health benefits. The Company offers over 110 flavors of frozen yogurt, ice cream, frozen custard, sorbet, smoothies, frozen carbonated beverages, slushes and frozen drink mixes. In addition to the YoCream brand, the Company also provides other branded flavors such as Hershey'sTM (e.g. Hershey'sTM KissesTM, Reese'sTM, YorkTM, Jolly RancherTM, TwizzlersTM, Bubble YumTM) and RockstarTM under exclusive licenses. Due to the nature of these products, sales are subject to seasonal fluctuations, with the summer months normally being the busiest season. The introduction and roll out of new products and growth in new market segments results in spikes in business which the Company views as normal operations.

YoCream sells its products primarily to a broad range of foodservice customers including frozen yogurt shops, convenience stores, warehouse stores, quick service restaurants, colleges, healthcare facilities, restaurants, and military and government foodservice locations. The Company's products are sold domestically and internationally through a strong and growing network of over 250 brokers and distributors to these thousands of retailers.

The Company has achieved outstanding growth in sales and earnings over the last several years. Fiscal year 2009 sales increased 18.1% to \$50,733,000, and fiscal year 2008 sales increased 52.4%, which were preceded by two additional years of double digit growth. Net income reached a record level of \$5,639,000 in 2009 compared with \$4,380,000 in 2008.

Frozen dessert sales for the fiscal year increased to \$41,873,000 versus \$32,140,000 a year ago. The 30.3% increase primarily resulted from exceptional growth in the Company's core frozen yogurt

products. Sales to a major national account that began in the second quarter of fiscal 2008 caught up with the prior years roll out and were lower in the last half of the year than the prior year. The Company continues to work with large national accounts, and four more are presently in test with different products.

Frozen beverage category sales for the year decreased to \$8,860,000 versus \$10,831,000 a year ago. The 18.2% decrease was primarily due to the Company not receiving the same number of flavor rotations for its frozen carbonated beverage (FCB) line in existing customer promotion schedules. In the second quarter one large frozen beverage customer chose to move to dual suppliers; however YoCream continues to enjoy a major part of the volume. The Company anticipates future growth in the frozen beverage category with the introduction of new products and access to new accounts.

The Fiscal 2009 frozen dessert growth of 30.3% is significant, especially in a recessed economy. Renewed demand for frozen yogurt has emerged from California and is growing rapidly in the Northeast, Southeast, Southwest, and Midwest as well as in international markets. Many of the smaller regional chains have and are expanding to other areas of the country. Frozen yogurt shops, especially self serve, are becoming destination points for consumers of all demographics. Most shops offer 10 to 20 soft serve flavors. YoCream was prepared to meet this demand with a high quality, diverse product line: Sweet profile frozen yogurts, including the Hershey's™ branded flavors; tart profile frozen yogurts; no-sugar-added frozen yogurts; sorbet, ice cream and frozen custard. More than 70 YoCream soft serve products allow operators to present an array of flavors that appeal to consumers of all ages and genders in every region of the country.

With this growth, the question of sustainability has been posed. Frozen yogurt and probiotic products are entrenched in the American diet and economy. YoCream anticipates its success in this market to be long term, based on the following factors: Product integrity, growing consumer awareness of probiotics, innovation and preparedness.

YoCream's profitable results follow the focus on achievement and the passion and dedication put forth in day-to-day operations. The high standard of business ethics is evident also in the integrity of YoCream products. YoCream has a long history of producing fine frozen yogurt products with high probiotic culture counts, distinguishing them from a number of competitive brands. YoCream frozen yogurt far exceeds the culture requirements set forth by the National Yogurt Association and the Company displays the Live and Active Cultures (LAC) seal on these products to help consumers identify them as real frozen yogurt.

Consumer interest and awareness of probiotic products and frozen yogurt continues to rise. In a survey conducted by IFIC Functional Foods, consumer awareness and consumption of probiotics for the health benefit of maintaining a healthy digestive system increased from 58% in 2007 to 72% in 2009. These results are mirrored in the consumer and operator calls that are fielded at YoCream asking about live and active cultured frozen yogurt. Milk is still the best media for probiotics and YoCream manufactures true yogurt with high levels of live and active probiotic cultures for the Company's frozen yogurt.

This new plateau of product awareness has been reached and the innovation possibility is endless. YoCream is in development on creative new products with potential customers in different market segments, like quick service restaurants and healthcare. New flavor development is a continual priority. In preparation for 2010, the Company introduced four new Original Tart™ frozen yogurt flavors in Q4 2009, three new frozen beverage flavors in Q4 2009, and two new sweet profile frozen yogurt flavors in Q1 2010. The R&D team is also working on probiotic products in new beverage and hardpack formats.

In March of 2009, the Company opened its YoCream Frozen Yogurt Company Store and Showroom in Portland, Oregon. The retail operation is located in a lifestyle mall near the Portland International Airport and the manufacturing facility. This product and marketing innovation center is a self serve frozen yogurt

outlet with full service frozen yogurt shakes and smoothies. The shop is an excellent resource for the Company's product development team, offering instant consumer feedback on new flavors. The showroom is also used for customer training, marketing research and as a sales tool. The Company showroom is not designed and operated to compete with YoCream customers but to increase product and brand awareness and promote the sale of YoCream products through the retailers it currently serves.

YoCream's innovative activities include more than the development of new products. In response to the flood of inquiries from potential new operators all over the country, the Company developed YoCream University, an innovative and intensive 2-day conference on starting and operating a frozen yogurt business. The conference has been offered monthly since August 2009 and covers topics such as: Concept Development, Frozen Yogurt 101, Food Safety, Financial Planning, Day-to-Day Operations, Staffing and Marketing. As a leader in the frozen yogurt market, YoCream felt it was important to provide new operators with knowledge and tools to help them become solid, sustainable operators and good stewards of real frozen yogurt. As a recent attendee noted, *"This was both an informative and enlightening course...prepares you well for embarking on a new business founded on Frozen Yogurt. YoCream staff are open and truly willing to help entrepreneurs."* -Bruno Eddy, Virginia, Graduate '09

YoCream's effective response to the surge in market demand for frozen yogurt was facilitated by its continued investment in plant and equipment. Over the past four fiscal years, YoCream has invested \$17.6 million in five facility upgrade and enhancement projects. YoCream has also been sensitive to its corporate responsibility to environmental sustainability evidenced by its energy efficiency projects resulting in carbon footprint reduction of over 1.1 million pounds per year or the equivalent of planting 152 acres of trees.

Gross profit for fiscal 2009 increased 27.4% to \$23,353,000. As a percentage of sales, gross profit margins for fiscal 2009 were 46.0% compared with 42.7% in 2008. The increase in gross profit margins was primarily due to economies of scale.

Distribution expenses include both freight and storage costs. Distribution expenses for fiscal 2009 decreased to 9.3% of sales, compared with 10.8% of sales in 2008. The reduction in distribution expenses as a percentage of sales in 2009 was achieved as a result of freight efficiencies, lower freight rates, and an increase in the number of customer pickups. Fuel surcharges remain high but were relatively flat for the year on average.

Sales and marketing expenses for fiscal 2009 as a percentage of sales were relatively flat at 7.4%, compared to 7.3% of sales in 2008.

General and administrative expenses for fiscal 2009 increased to 8.1% of sales compared to 6.9% of sales in 2008. The increase as a percentage of sales primarily relates to an increase in personnel costs. Management expects that general and administrative expenses will not increase in fiscal 2010.

Income from operations for fiscal 2009 increased 41.5% to \$10,781,000 from \$7,621,000 in 2008. As a percentage of sales, income from operations in 2009 increased to 21.3% compared with 17.7% in 2008. The increase was due to the increase in sales and the economies of scale resulting in reduced operating costs and expenses as a percent of sales. The Company expects the positive sales trend to continue as a result of its new product introductions and intense sales activity.

Restricted stock compensation in fiscal 2009 increased over 2008 due to the Board of Directors approved modifications to the 2005 and 2006 Restricted Share Awards that vested the remaining shares based on considerations of both past and current results. Additional restricted stock compensation is not planned or anticipated at this time.

The effective tax rate in fiscal 2009 was 35.5% compared with 34.7% in 2008.

Net income for fiscal year 2009 was \$5,639,000, or \$2.24 per share compared with \$4,380,000, or \$1.89 per share in 2008. Net income as a percentage of sales, was 11.1% in 2009 compared with 10.2% in 2008.

Earnings before interest, taxes, depreciation and non-cash restricted stock compensation (EBITDA) for fiscal 2009 increased 37.5% to \$11,793,000 compared with \$8,575,000 in 2008. EBITDA, as a percentage of sales was 23.2% in 2009 compared with 20.0% in 2008.

Liquidity and Capital Resources

In recent years, the Company has financed its operations and expansion from internally generated funds, bank loans, industrial revenue bonds and operating leases.

As presented in the Statement of Cash Flows, the Company's successful performance in fiscal 2009 resulted in cash and cash equivalents increasing by \$4,949,000 to \$12,118,000 at October 31, 2009.

The Company has an unutilized bank line of credit of \$3,000,000, which matures in July 2010. In addition, the Company has an unutilized unsecured revolving line of credit which provides the option to borrow an additional \$1,000,000. In conjunction with the 2009 annual renewal of the Company's lines of credit, the terms of the additional unsecured revolving line of credit were modified to remove the borrowing limitations based on the levels of eligible receivables and inventory.

At October 31, 2009 and 2008, the Company had working capital of approximately \$15,877,000 and \$7,806,000 respectively.

The Company believes its existing assets, bank lines, and cash flow from operations will be sufficient to fund the Company's operations for at least the next twelve months.

Off Balance Sheet Arrangements

Through fiscal year 2009, the Company has entered into operating leases relating to certain assets utilized in its production process. (See Note M of the Notes to Financial Statements for a description of these off-balance sheet lease commitments.) The Company also leases its offices, production facility and warehouse from a related party with terms of 15 to 40 years. (See Notes M and O of Notes to Financial Statements for a description of the terms).

Subsequent Event

In November 2009, the Company declared a special one-time dividend of \$2 per share paid on December 1, 2009 to shareholders of record as of the close of business on November 17, 2009. Total dividends paid approximate \$5,216,000.

5. Legal proceedings

Not applicable

6. Defaults upon senior securities

Not applicable

7. Other information

Not applicable

9. Certifications

I, John N. Hanna, certify that:

1. I have reviewed this annual report for YoCream International, Inc.
2. Based on my knowledge, this disclosure statement does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this disclosure statement; and
3. Based on my knowledge, the financial statements, and other financial information included or incorporated by reference in this disclosure statement, fairly present in all material respects the financial condition, results of operations and cash flows of the issuer as of, and for, the periods presented in this disclosure statement.

January 29, 2010

By:



John N. Hanna
Chairman and Chief Executive Officer

I, W. Douglas Caudell, certify that:

1. I have reviewed this annual report for YoCream International, Inc.
2. Based on my knowledge, this disclosure statement does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this disclosure statement; and
3. Based on my knowledge, the financial statements, and other financial information included or incorporated by reference in this disclosure statement, fairly present in all material respects the financial condition, results of operations and cash flows of the issuer as of, and for, the periods presented in this disclosure statement.

January 29, 2010

By:



W. Douglas Caudell
Chief Financial Officer

January 29, 2010

To Our Shareholders, Customers and Suppliers:

“Is it sustainable?” That’s the question inevitably hurled at us when our gratifying financial results are presented. Our modest answer is “yes!” Here are some of the reasons for our confidence.

Public awareness of probiotic benefits continues to grow, creating demand for our enjoyable frozen yogurt and smoothie products. YoCream is well known for advocating products with high live and active culture counts.

Frozen yogurt shops, owned or franchised by savvy investors, proliferate throughout the nation. These shops are unique, offering consumers a variety of product configurations. Many of these stores have become destination points for meeting friends and having fun. YoCream is the industry leader in providing products, flavors, and marketing concepts for these shops and chains.

Quick service restaurants recognize that most Americans want better, healthier choices for their favorite menu items, prompting restaurant chain interest in yogurt concepts. YoCream is at the forefront in responding to this sizeable market.

International interest in our products is indicative of an expanding marketplace. YoCream is now selling in twelve nations and is developing a product model that is expected to facilitate increased sales abroad.

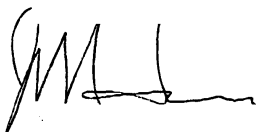
Innovative applications of frozen yogurt seem exhaustless, creating many opportunities with both existing and new customers. YoCream’s R&D personnel are the most experienced specialized team available.

Our thirty-four year record speaks for itself relative to viability in both lean and prosperous times. YoCream’s management and key employees, most of whom have been with the Company for many years, know how to tough it out and work together to meet the challenge at hand.

So we remain positive about the prospects ahead.

While we recognize the need for continued growth and profitability, we are also sensitive to other business responsibilities. Food safety is primary; we continue to maintain the highest quality assurance standards. Concern for environmental sustainability is a focus, evidenced by our plant and equipment upgrades. Integrity and transparency are espoused and these values are a requirement for employment.

The Board of Directors was pleased to recognize our investors by issuing a special dividend. All of our hard working employees were rewarded with reasonable bonuses. It was a very good year. We look ahead to new achievements.



John N. Hanna
Chief Executive Officer

YOCREAM INTERNATIONAL, INC.

FINANCIAL STATEMENTS

INDEPENDENT AUDITOR'S REPORT

To the Board of Directors
of YoCream International, Inc.
Portland, Oregon

We have audited the accompanying balance sheets of YoCream International, Inc. as of October 31, 2009 and 2008, and the related statements of income, changes in shareholders' equity, and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of YoCream International, Inc. as of October 31, 2009 and 2008, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

Mack, Roberts & Co., LLC
Mack, Roberts & Co., LLC
Portland, Oregon

January 29, 2010



YOCREAM INTERNATIONAL, INC.

BALANCE SHEETS

October 31

	<u>2009</u>	<u>2008</u>
ASSETS		
Current assets		
Cash and cash equivalents	\$ 12,118,067	\$ 7,169,393
Accounts receivable, net of allowance for doubtful accounts of \$61,400 in 2009 and \$43,400 in 2008	2,542,618	2,346,555
Inventories	5,151,899	3,614,226
Income tax receivable	100,248	-
Other current assets	569,775	346,722
Deferred tax assets	<u>243,775</u>	<u>218,877</u>
Total current assets	20,726,382	13,695,773
Fixed assets, net	14,712,748	14,297,886
Intangible and other long-term assets, net	1,196,655	1,108,290
Deferred tax assets	<u>309,500</u>	<u>191,900</u>
	<u>\$ 36,945,285</u>	<u>\$ 29,293,849</u>
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities		
Note payable – line of credit	\$ -	\$ -
Current portion of long-term debt	647,873	616,155
Accounts payable	3,440,694	2,661,073
Income tax payable	-	1,778,606
Other accrued liabilities	<u>761,085</u>	<u>833,459</u>
Total current liabilities	4,849,652	5,889,293
Long-term debt, less current portion	7,378,449	7,720,045
Deferred tax liabilities	2,144,975	1,344,077
Other liabilities	<u>145,250</u>	<u>119,376</u>
Total liabilities	<u>14,518,326</u>	<u>15,072,791</u>
Shareholders' equity		
Preferred stock, no par value, 5,000,000 shares authorized, none issued or outstanding		-
Common stock, no par value, 30,000,000 shares authorized	7,750,865	6,618,865
Unearned compensation – restricted stock	-	(1,623,830)
Retained earnings	15,172,494	9,533,723
Accumulated other comprehensive income	<u>(496,400)</u>	<u>(307,700)</u>
Total shareholders' equity	<u>22,426,959</u>	<u>14,221,058</u>
	<u>\$ 36,945,285</u>	<u>\$ 29,293,849</u>

YOCREAM INTERNATIONAL, INC.

STATEMENTS OF INCOME
For the years ended October 31,

	<u>2009</u>	<u>2008</u>
Sales	\$ 50,732,601	\$ 42,971,072
Cost of goods sold	<u>27,379,128</u>	<u>24,628,048</u>
Gross profit	23,353,473	18,343,024
Operating costs and expenses		
Distribution expenses	4,731,364	4,623,787
Selling and marketing expenses	3,751,978	3,142,396
General and administrative expenses	<u>4,089,206</u>	<u>2,955,925</u>
Income from operations	10,780,925	7,620,916
Other income (expense)		
Interest income	28,505	23,522
Interest expense	(443,829)	(529,602)
Restricted stock compensation	<u>(1,623,830)</u>	<u>(411,170)</u>
Income before income taxes	8,741,771	6,703,666
Income tax provision	<u>3,103,000</u>	<u>2,324,000</u>
Net income	<u>\$ 5,638,771</u>	<u>\$ 4,379,666</u>
Earnings per common share - basic	<u>\$2.31</u>	<u>\$1.99</u>
Earnings per common share - diluted	<u>\$2.24</u>	<u>\$1.89</u>
Shares used in basic earnings per share	<u>2,445,856</u>	<u>2,200,753</u>
Shares used in diluted earnings per share	<u>2,511,725</u>	<u>2,323,198</u>

YOCREAM INTERNATIONAL, INC.

STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY

	Shares	Amounts	Unearned Compensation - Restricted Stock	Retained Earnings	Accumulated Other Comprehensive Income	Total Shareholders' Equity
Balance, October 31, 2007	2,174,606	\$ 6,426,965	\$ (2,035,000)	\$ 5,154,057	\$ (162,300)	\$ 9,383,722
Comprehensive income:						
Net income	-	-	-	4,379,666	-	4,379,666
Change in fair value of derivative financial instruments, net of income taxes of (\$90,800)	-	-	-	-	(145,400)	(145,400)
Comprehensive income						4,234,266
Stock options exercised	5,000	23,150	-	-	-	23,150
Common stock purchased	(5,000)	(46,250)	-	-	-	(46,250)
Restricted stock vested	87,604	-	411,170	-	-	411,170
Excess tax benefit of restricted stock vested	-	215,000	-	-	-	215,000
Balance, October 31, 2008	2,262,210	\$ 6,618,865	\$ (1,623,830)	\$ 9,533,723	\$ (307,700)	\$ 14,221,058
Comprehensive income:						
Net income	-	-	-	5,638,771	-	5,638,771
Change in fair value of derivative financial instruments, net of income taxes of (\$117,600)	-	-	-	-	(188,700)	(188,700)
Comprehensive income						5,450,071
Restricted stock vested	345,688	-	1,623,830	-	-	1,623,830
Excess tax benefit of restricted stock vested	-	1,132,000	-	-	-	1,132,000
Balance, October 31, 2009	<u>2,607,898</u>	<u>\$ 7,750,865</u>	<u>\$ -</u>	<u>\$ 15,172,494</u>	<u>\$ (496,400)</u>	<u>\$ 22,426,959</u>

YOCREAM INTERNATIONAL, INC.

STATEMENTS OF CASH FLOWS

For the years ended October 31,

	<u>2009</u>	<u>2008</u>
Cash flows from operating activities		
Net income	\$ 5,638,771	\$ 4,379,666
Adjustments to reconcile net income to net cash provided by operating activities		
Depreciation and amortization	1,012,203	954,034
Deferred income taxes	776,000	113,000
Change in assets and liabilities		
Accounts receivable	(196,063)	(783,600)
Inventories	(1,537,673)	134,299
Other assets	(311,418)	(31,059)
Accounts payable	598,947	1,044,606
Income taxes receivable (payable)	(1,878,854)	1,652,724
Restricted stock compensation	1,623,830	411,170
Other accrued liabilities	<u>(46,500)</u>	<u>378,307</u>
Net cash provided by operating activities	<u>5,679,243</u>	<u>8,253,147</u>
Cash flows from investing activities		
Proceeds from sale and lease back of equipment	3,714,467	1,000,314
Expenditures for fixed assets	<u>(4,960,858)</u>	<u>(1,336,593)</u>
Net cash used in investing activities	<u>(1,246,391)</u>	<u>(336,279)</u>
Cash flows from financing activities		
Payments on line of credit	-	(634,475)
Proceeds from long-term debt	-	90,000
Proceeds from development grant	-	90,000
Proceeds from stock options	-	23,150
Repurchase of common stock	-	(46,250)
Principal payments on long-term debt	(616,178)	(555,601)
Excess tax benefits of restricted stock and options	<u>1,132,000</u>	<u>215,000</u>
Net cash provided by (used in) financing activities	<u>512,822</u>	<u>(818,176)</u>
Net increase in cash and cash equivalents	4,948,674	7,098,692
Cash and cash equivalents, beginning of year	<u>7,169,393</u>	<u>70,701</u>
Cash and cash equivalents, end of year	<u>\$ 12,118,067</u>	<u>\$ 7,169,393</u>

YOCREAM INTERNATIONAL, INC.

NOTES TO FINANCIAL STATEMENTS

NOTE A - OPERATIONS AND SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

YoCream International, Inc., with headquarters and manufacturing facility in Portland, OR, was founded in 1977. The Company produces, markets and sells frozen yogurt, ice cream and frozen custard mixes as well as fruit and dairy smoothies and frozen beverages. The Company is an established food service vendor and private label co-packer with a proven history of providing high-quality products and solution-based customer service.

On January 3, 2006, the Company filed Form 15 with the Securities and Exchange Commission to provide notice of the voluntary termination of its registration under Section 12(g) of Securities and Exchange Act of 1934 due to the number of shareholders being under 300. Concurrently the Company also voluntarily delisted its shares with NASDAQ. Several significant shareholders recommended that the Company consider alternatives to reduce the escalating costs of being registered with the SEC. The Board of Directors took this recommendation into consideration and decided that voluntarily delisting was the most cost effective alternative, as well as allowing management to intensify its focus on business opportunities. The Company's stock is currently listed on the Pink Sheets.

1. Significant Estimates

In preparing financial statements in conformity with accounting principles generally accepted in the United States of America, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the date of the financial statements and revenues and expenses during the reporting period. Actual results could differ from those estimates.

2. Cash and cash equivalents

Cash and cash equivalents include money market, certificate of deposit, and U.S. Treasury bill investments with a remaining maturity of nine months or less when purchased. The Company maintains cash balances at several banks. All accounts are fully insured by the Federal Deposit Insurance Corporation.

3. Accounts receivable

The majority of the Company's accounts receivable are due from companies in the retail and wholesale food service industries. Credit is extended based on evaluation of a customers' financial condition and, the Company periodically performs credit evaluations of its customers. Credit insurance is obtained on selected accounts. Accounts receivable are generally due within 15 days and are stated at amounts due from customers net of an allowance for doubtful accounts. Accounts outstanding longer than the contractual payment terms are considered past due. The Company determines its allowance by considering a number of factors, including the length of time trade accounts receivable are past due, the Company's previous loss history, the customers' current ability to pay its obligation to the Company, and the condition of the general economy and the industry as a whole. The Company writes-off accounts receivable when they become uncollectible, and payments subsequently received on such receivables are credited to the allowance for doubtful accounts. Historically the Company's credit losses have been insignificant.

YOCREAM INTERNATIONAL, INC.

NOTES TO FINANCIAL STATEMENTS

4. Inventories

Inventories are stated at the lower of cost or market. The Company determines cost based on the first-in, first-out (FIFO) method for raw materials, packaging materials and supplies, and based on standard costs for finished goods, which approximates cost based on the first-in, first-out method. The allocation of fixed production overheads are based on the normal capacity of the production facilities. Abnormal amounts of idle facilities, freight, handling costs, and spoilage are recognized as charges of the current period.

5. Fixed Assets

Fixed assets are stated at cost. Expenditures for replacements and improvements are capitalized, and expenditures for repairs and maintenance and routine replacements are charged to operating expense as incurred. When assets are sold or otherwise disposed of, the cost and related accumulated depreciation are eliminated from the accounts and any resulting gain or loss is included in operations. Depreciation is provided for on a straight-line basis in amounts sufficient to relate the cost of depreciable assets to operations over their estimated service lives. Leasehold improvements are amortized over the life of the lease or the service life of the improvement, whichever is shorter. Property, plant and equipment are reviewed for impairment whenever events or circumstances indicate that the carrying amount of assets may not be recoverable. If such assets are considered to be impaired, the impairment to be recognized is measured as the amount by which the carrying amount of the assets exceeds the fair value of the assets. The estimated lives used in calculating depreciation and amortization are as follows:

Plant facilities expansion	40 years
Plant equipment	10-25 years
Office equipment and furnishings	3-10 years
Leasehold improvements	5-14 years

6. Financial Instruments

The carrying values of cash and cash equivalents, accounts receivable and payable, approximate fair value because of the relatively short maturity of these instruments. The carrying value of notes payable and long-term debt approximate fair values based upon the interest rates available to the Company for similar instruments.

7. Other Comprehensive Income

Other comprehensive income, which is related to interest rate swaps at fair value, is accounted for in a manner as required by the Comprehensive Income Topic of the FASB Accounting Standards Codification (ASC).

8. Revenue Recognition and Sales Incentives

Revenue from the sale of products is generally recognized at the time of shipment to the customer. Certain promotional payments paid to wholesalers or retailers by the Company for the sale of its products is reported as a reduction of the revenues in the period they are provided. For the years ended October 31, 2009, and 2008 the total of rebates and promotional costs charged against sales were approximately \$2,106,000 and \$1,972,000, respectively.

YOCREAM INTERNATIONAL, INC.

NOTES TO FINANCIAL STATEMENTS

9. Shipping and Handling Costs

Shipping and handling fees and costs are separately classified as distribution expenses. Payments received from customers for shipping and handling costs are classified as part of net sales upon recognition of the related sale.

10. Research and Development Costs

Research and development costs are expensed as incurred. For the years ended October 31, 2009, and 2008 such costs aggregated approximately \$1,301,000 and \$937,000, respectively, and are classified in the financial statements as part of cost of sales, selling, general and administrative expenses, as appropriate.

11. Stock Based Compensation Plans

The Company has a stock-based employee compensation plan which is more fully described in Note K. The plan is accounted for in accordance with the provisions of the Stock Compensation Topic of the FASB ASC.

12. Earnings Per Share (EPS)

Basic EPS is computed using the weighted average number of shares of common stock outstanding for the period. Diluted EPS is computed using the weighted average number of shares of common stock and dilutive common stock equivalents outstanding during the period. Common equivalent shares from restricted stock are excluded from the computation when their effect is antidilutive.

13. Supplemental Cash Flow Information

Supplemental cash flow information for the years ended October 31, are as follows:

	<u>2009</u>	<u>2008</u>
Cash paid during the period for income taxes	\$ 3,074,000	\$ 343,000
Cash paid during the period for interest	\$ 488,000	\$ 491,000
Fair value of interest rate swap, net of taxes	\$ (188,700)	\$ (145,400)
Payment of vendor payables used to acquire capital assets	\$ 180,700	\$ -
Deferred taxes related to interest rate swap	\$ 117,600	\$ 90,800

14. Concentrations of Credit Risk and Major Customers

At October 31, 2008 one customer accounted for 41.7% of accounts receivable and 42.2% of gross sales. At October 31, 2009, this customer accounted for 31.9% of accounts receivable and 35.9% of gross sales.

At October 31, 2008 another customer accounted for 18.1% of accounts receivable and 13.7% of gross sales. At October 31, 2009, this customer accounted for 10.0% of accounts receivable and 14.4% of gross sales.

YOCREAM INTERNATIONAL, INC.

NOTES TO FINANCIAL STATEMENTS

At October 31, 2008 another customer accounted for 16.1% of accounts receivable and 14.0% of gross sales. At October 31, 2009, this customer accounted for 16.7% of accounts receivable and 20.6% of gross sales. This customer is a regional distributor utilized by the Company as a conduit to service over 1,000 of the Company's frozen yogurt customers.

The Company does not consider that these customers represent any credit risk.

NOTE B – ADOPTION OF ACCOUNTING PRONOUNCEMENTS

In June 2009, the FASB issued "The FASB Accounting Standards Codification and the Hierarchy of Generally Accepted Accounting Principles", which establishes the FASB Accounting Standards Codification ("ASC") as the source of authoritative accounting principles recognized by the FASB to be applied in preparation of financial statements in conformity with GAAP. The ASC is effective for financial statements issued for interim and annual periods ending after September 15, 2009. The Codification does not change or alter existing generally accepted accounting principles. The implementation had no impact to the Company's financial position or results of operations.

As of November 1, 2008, the Company adopted "Accounting for Uncertainty in Income Taxes — an interpretation of FASB Statement No. 109," which clarifies the accounting and disclosure for uncertainty in tax positions, as defined. Based on a review of its tax returns, the Company believes that its income tax filing positions and deductions would be sustained on audit and does not anticipate any adjustments that would result in a material change to its financial position. Therefore, no reserves for uncertain income tax positions have been recorded pursuant to the adoption. In addition, the Company did not record a cumulative effect adjustment related to the adoption of the standard. The Company's policy for recording any interest or penalties, if applicable, associated with audits would be to record such items as a component of income tax expense. There were no such items during the periods covered by this report.

NOTE C – COMPREHENSIVE INCOME

Comprehensive income is net income plus certain other items that are recorded directly to shareholder's equity. For the years ended October 31, 2009 and 2008, the change in fair value of derivative financial instruments, net of income taxes is the only component applied to net income to calculate the Company's comprehensive income.

NOTE D - INVENTORIES

Inventories consist of the following at October 31,:

	<u>2009</u>	<u>2008</u>
Finished goods	\$ 3,842,871	\$ 2,484,833
Raw materials	974,379	775,644
Packaging material and supplies	<u>334,649</u>	<u>353,749</u>
	<u>\$ 5,151,899</u>	<u>\$ 3,614,226</u>

YOCREAM INTERNATIONAL, INC.

NOTES TO FINANCIAL STATEMENTS

NOTE E - FIXED ASSETS

Fixed assets consist of the following at October 31,:

	<u>2009</u>	<u>2008</u>
Machinery and equipment	\$ 10,385,087	\$ 10,115,283
Plant facilities expansion	7,984,683	7,984,683
Leasehold improvements	2,308,585	1,818,795
Office equipment and furnishings	609,831	551,876
Construction in process	<u>416,770</u>	<u>264,183</u>
	21,704,956	20,734,820
Less accumulated depreciation	<u>(6,992,208)</u>	<u>(6,436,934)</u>
	<u>\$ 14,712,748</u>	<u>\$ 14,297,886</u>

For the year ended October 31, 2009, capitalized interest relating to a facility expansion project amounted to \$63,600. Payroll relating to the project was capitalized in the amount of \$75,600.

In fiscal 2007 the Company obtained approval from Portland Development Commission for a five-year enterprise zone property tax exemption on additions of real and personal property during the three year period from 2007 through 2009, subject to compliance with certain conditions. This property tax exemption was extended for three years in 2009.

NOTE F - INTANGIBLE AND OTHER LONG-TERM ASSETS

Intangible and other long-term assets consist of the following at October 31,:

	<u>2009</u>	<u>2008</u>
Other assets	\$ 80,096	\$ 8,268
Trademarks	108,733	108,733
Lease deposits (see Note O)	330,013	330,013
Bond financing costs (see Note G)	326,248	336,657
Insurance policy premium advances (see Note O)	<u>351,565</u>	<u>324,619</u>
	<u>\$ 1,196,655</u>	<u>\$ 1,108,290</u>

YOCREAM INTERNATIONAL, INC.

NOTES TO FINANCIAL STATEMENTS

NOTE G – CURRENT AND LONG-TERM DEBT

In December 2003, the Company finalized the terms of the master finance lease facility in the amount of \$2,952,553. The facility provides for payments over seven years with interest at 30-day LIBOR plus 175 basis points. In November 2004, the Company exercised its option to enter into a swap arrangement to fix the rate at 5.88% for the term of the lease. The facility is collateralized by the initial aseptic system project assets, and by certain other equipment and fixtures.

On October 30, 2006, the Company closed the financing of multi-mode variable rate industrial revenue bonds in the amount of \$6,700,000. On January 4, 2007, the bonds were converted to tax-exempt bonds that provide for monthly interest payments at a weekly floating rate, which was 1.04% at October 31, 2009. The Company also entered into a ten-year swap arrangement, which provided for a rate of 4.08%, less 71% of the one month LIBOR rate (.18% at October 31, 2009, which has historically approximated the tax-exempt floating rate). At October 31, 2009 the overall effective rate was approximately 4.94%. Principal payments began February 1, 2008 and continue in varying amounts through February 1, 2038. The bonds are secured by a direct pay letter of credit provided by KeyBank National Association, which provides for an annual fee of 1.35% of the bonds outstanding. The direct pay letter of credit is for a rolling period of five years and is subject to review and extension each year. Due to the unusual events that affected the credit markets in the past year, the cost of extending the direct pay letter of credit was not feasible in October 2009. It was determined by all parties involved that a fifth year would not be added this year. It is expected that the term will be extended to the original five years at the upcoming renewal date in October 2010. The collateral for the direct pay letter of credit is a reimbursement agreement, leasehold deed of trust on one of the parcels of property leased by the Company, an assignment of the lease on the other parcel leased by the Company, and a security interest in certain equipment with a cost of \$1,345,000, which was financed with bond proceeds.

In March 2007, the Company arranged financing for certain technology equipment, and software. At October 31, 2008 the balance on the line was \$139,000. In January 2009 this financing arrangement was converted to a two year term note with interest at prime plus 1.00%. The collateral for the term note is a security interest in certain technology equipment.

In November 2007, the Company closed a financing arrangement with the Portland Development Commission, which provides a grant of \$90,000 and a loan of \$90,000. The loan does not require any interest or principal payments during the first two years. The remaining term is 7 years, with payments based on a 20 year amortization schedule and a low interest rate to be determined in February 2010 based on employment additions. The financing was arranged in conjunction with adding a new energy efficient roof on the main plant building.

The Company has an unsecured bank line of credit which permits borrowing up to \$3,000,000. The line bears interest at the bank's commercial lending rate, 3.25% at October 31, 2009. The line is subject to renewal by July 2010. There were no amounts drawn on this line at October 31, 2009.

The Company also has an unsecured revolving bank line of credit that permits borrowing an additional \$1,000,000 with the same interest rate and maturity as described above. In conjunction with the 2009 annual renewal of the Company's bank line of credit, the provisions of this facility were modified to remove the borrowing limitations previously based on levels of eligible receivables and inventory.

The bank line of credit, master finance lease, and reimbursement agreement related to the bond financing all contain the same financial covenants, including ones related to the ratio of senior liabilities (as defined)

YOCREAM INTERNATIONAL, INC.

NOTES TO FINANCIAL STATEMENTS

to adjusted tangible capital, current ratio and operating cash flow to fixed charge as well as limits on the amount of common stock which can be repurchased by the Company. At October 31, 2009, the Company was in compliance with all of these ratios and covenants.

Long-term debt consists of the following at October 31,:

	<u>2009</u>	<u>2008</u>
Multi-mode industrial revenue bonds; with interest payable monthly based on the terms of a swap agreement that matures October 30, 2016; principal payable annually in various amounts beginning February 2008 through 2038; secured by a direct pay letter of credit, which is collateralized by a leasehold deed of trust on one lot, an assignment of lease on the other lot, and by a security interest in certain equipment financed with bond proceeds	\$ 6,470,000	\$ 6,585,000
Interest rate swap fair value	791,700	480,400
Master finance lease obligation to a bank; payable in monthly installments of \$38,880 through January 2011, plus interest at a 30 day LIBOR plus 1.75% (1.99% and 4.92% at October 31, 2009 and 2008); variable rate adjusts to a rate of 5.88%, which is fixed through a swap agreement that matures in 2011; collateralized by certain equipment financed with lease proceeds	572,077	1,015,058
Interest rate swap fair value	14,200	19,200
Term loan to a bank, payable in monthly installments of \$6,066, including interest at prime plus 1.00% (4.25% and 5.00% at October 31, 2009 and October 31, 2008) through December 2010; collateralized by certain equipment	88,345	139,393
Term loan, payable in monthly installments beginning April 1, 2010, including interest at a nominal rate to be determined based on employment levels, with final maturity in November 2017; collateralized by certain equipment	90,000	90,000
Note payable in monthly installments of \$913 through June 2009, including interest at 5.25%; collateralized by certain equipment	-	7,149
	<u>8,026,322</u>	<u>8,336,200</u>
Less portion due within one year	<u>(647,873)</u>	<u>(616,155)</u>
	<u>\$ 7,378,449</u>	<u>\$ 7,720,045</u>

YOCREAM INTERNATIONAL, INC.

NOTES TO FINANCIAL STATEMENTS

Maturities of long-term debt are as follows:

<u>Year ending October 31,</u>	
2010	\$ 647,873
2011	260,743
2012	132,152
2013	137,262
2014	142,379
Thereafter	5,900,013
Plus interest rate swap fair value	<u>805,900</u>
	<u>\$ 8,026,322</u>

NOTE H – FAIR VALUE OF DERIVATIVE FINANCIAL INSTRUMENTS

In October 2006, the Company entered into an interest rate swap agreement relating to the multi-mode industrial revenue bonds, which converted the variable interest rate to a tax-exempt “fixed” rate of 4.08%, as described in Note G. This agreement will terminate on October 30, 2016. The mark-to-market adjustments were \$791,700 and \$480,400, and the related tax effects were \$(304,000) and \$(184,500) at October 31, 2009 and 2008, respectively.

In November 2004, the Company entered into an interest rate swap agreement relating to the master finance lease obligation, which converted the variable interest rate paid on its debt to a fixed rate of 5.88%. This agreement will terminate on January 1, 2011. The mark-to-market adjustments were \$14,200 and \$19,200, and the related tax effect was \$(5,500) and \$(7,400), at October 31, 2009 and 2008, respectively.

It is the Company’s policy to enter into agreements when management deems them useful in reducing risks to the Company. To the extent that the fixed rate is higher than the interest rates provided for in the lease or bond facilities, payment is due from the Company for the difference. To the extent that the fixed rate is below the interest rates provided for in the lease or bond facilities, the Company is entitled to receive the difference. As required by the Derivatives and Hedging Topic of the FASB ASC, the Company has reviewed and designated its interest rate swap agreement as a cash flow hedge and recognizes the fair value of its interest rate swap agreement on the balance sheet. Changes in the fair value of this agreement are recorded, net of taxes, in accumulated other comprehensive income. The hedge ineffectiveness, if any, is recorded in earnings..

NOTE I- ADVERTISING COSTS

Advertising costs are charged to operations in the year incurred. For the years ended October 31, 2009 and 2008 advertising costs aggregated approximately \$782,000 and \$655,000, respectively.

NOTE J - EMPLOYEE BENEFIT PLANS

The Company has a 401(k) Employee Savings Plan and Trust (the Plan) which requires the Company to make contributions to the Plan in the amount of 3% of eligible employee compensation. The Plan allows that the required contributions may be invested in common stock of the Company. The Company made

YOCREAM INTERNATIONAL, INC.

NOTES TO FINANCIAL STATEMENTS

contributions to the Plan of approximately \$159,000 and \$176,000 during the years ended October 31, 2009 and 2008, respectively. All such contributions have been made in the form of common stock of the Company, which has been purchased on the open market. Employees who have met the eligibility requirements are required to contribute a minimum amount to the Plan, subject to certain Internal Revenue Code requirements. In addition, employees may elect to sell the contributed common stock of the Company and request that the proceeds be transferred to their own account in the Plan.

Additionally, the Company has a profit-sharing plan for eligible employees. Under the provisions of the plan, the Company may, at its discretion, make contributions of a sum not in excess of the amount permitted under the Internal Revenue Code as a deductible expense. The Company has not made any contributions to this plan.

NOTE K - STOCK INCENTIVE PLAN

In April 2005, the shareholders approved the amendment and restatement of the Company's 2000 Stock Option Plan. The plan was renamed the 2005 Stock Incentive Plan; and was amended to provide for stock settled SARs, performance share awards, restricted share awards and nonqualified stock options as the types of equity awards that may be granted to employees, non-employee directors and other persons who contribute to the long-term success of the Company. The total number of shares authorized for grants under the stock incentive plan was also increased from 400,000 to 650,000. The plan will terminate February 25, 2015.

A summary of option transactions relating to the Stock Incentive Plan is as follows:

	<u>Shares Under Option</u>	<u>Weighted Average Exercise Price</u>
Balance, October 31, 2007 (average remaining life 0.8 years)	5,000	\$4.63
Options exercised	<u>(5,000)</u>	
Balance, October 31, 2008	<u><u>-</u></u>	

On September 19, 2005, restricted shares of common stock aggregating 300,000 shares were awarded, to directors, officers and senior managers pursuant to the terms of the 2005 Stock Incentive Plan. The shares vest ratably equal to one-seventh of the original grant on the anniversary date of the award. The related compensation cost will be recognized as the shares vest. The fair value on the date of the award was \$5.00 per share. In 2008, 42,854 of the above shares vested, and compensation expense of \$214,300 was recognized. At October 31, 2008, 171,438 shares relating to this award were not vested.

On June 23, 2006, the Board of Directors approved conversion of stock options previously granted to directors, officers and senior managers for 255,000 shares of common stock to awards of restricted shares of common stock on a one-for-one basis. Vesting of such restricted stock is based on a combination of performance and time vesting criteria. The related compensation cost will be recognized as the shares vest. The fair value on the date of the award was \$4.40 per share. At October 31, 2008, 174,250 shares relating to this award were not vested.

On February 28, 2009, 63,750 restricted shares vested under the 2006 award and the related compensation expense was \$280,500.

YOCREAM INTERNATIONAL, INC.

NOTES TO FINANCIAL STATEMENTS

Effective May 1, 2009, the Board of Directors approved modifications in the 2005 and 2006 restricted share awards, which resulted in the vesting of the remaining 281,938 shares and the related restricted stock expense was \$1,343,390. The modifications took into consideration both past performance and the expected results for the fiscal year.

A summary of the above shares vesting and related compensation expense for the years ended October 31, is as follows:

	<u>2009</u>	<u>2008</u>
Shares vesting	345,688	87,604
Compensation expense	\$ 1,623,830	\$ 411,170

At October 31, 2009 and 2008, there were 15,000 shares of common stock available for issuance under the Company's stock incentive plan.

NOTE L - INCOME TAXES

The provision for income taxes for the years ended October 31, consists of the following:

	<u>2009</u>	<u>2008</u>
Current	\$ 2,327,000	\$ 2,211,000
Deferred	<u>776,000</u>	<u>113,000</u>
	<u>\$ 3,103,000</u>	<u>\$ 2,324,000</u>

The effective tax rate differed from the statutory federal tax rate for the years ended October 31, due to the following:

	<u>2009</u>	<u>2008</u>
Statutory federal tax rate (graduated)	34.0%	34.0%
State taxes, net of federal benefit	1.7	3.6
State and federal tax credits	(2.0)	(1.4)
Other	<u>1.8</u>	<u>(1.5)</u>
	<u>35.5%</u>	<u>34.7%</u>

YOCREAM INTERNATIONAL, INC.

NOTES TO FINANCIAL STATEMENTS

Deferred tax assets (liabilities) consist of the following at October 31,:

	<u>2009</u>	<u>2008</u>
Current deferred tax assets		
Accrued expenses	\$ 47,700	\$ 43,200
Allowance for doubtful accounts	23,600	16,700
State credits carryforward	65,500	70,700
Other	<u>106,975</u>	<u>88,277</u>
Deferred tax assets	243,775	218,877
Non-current deferred tax assets		
Mark-to-market effect	<u>309,500</u>	<u>191,900</u>
	<u>\$ 553,275</u>	<u>\$ 410,777</u>
Deferred tax liabilities		
Fixed assets	<u>\$ (2,144,975)</u>	<u>\$ (1,344,077)</u>

State energy tax credits expire in 2013.

NOTE M - OPERATING LEASE COMMITMENTS

The Company leases its production, warehouse and office facilities under operating lease agreements with related parties (see Note O). The Company also leases a warehouse, and equipment under non-cancelable operating leases with unrelated third parties.

Minimum lease payments required under these operating leases are as follows:

<u>Year ending October 31,</u>	
2010	\$ 1,794,000
2011	1,815,000
2012	1,833,000
2013	2,968,000
2014	682,000
Thereafter	<u>10,718,000</u>
	<u>\$ 19,810,000</u>

Operating lease expense for the years ended October 31, 2009 and 2008 approximated \$1,248,000 and \$800,000, respectively. Operating lease expenses are allocated between manufacturing costs, general and administrative, and sales and marketing expenses in the accompanying statements of income.

YOCREAM INTERNATIONAL, INC.

NOTES TO FINANCIAL STATEMENTS

In October 2008, the Company entered into a sale-leaseback arrangement. Under this arrangement, the Company sold certain manufacturing equipment for \$1,000,314 and leased it back for a period of five years. The lease has been accounted for as an operating lease. There was no gain on the transaction.

In October 2008, the Company amended an existing lease on warehouse facilities to expand its storage for raw materials. The lease is for a period of five years.

In December 2008, the Company entered into a lease for a retail showroom space in a nearby shopping center. The lease is for a period of ten years.

In April 2009, the Company entered into a sale-leaseback arrangement. Under this arrangement, the Company sold certain manufacturing equipment for \$438,000 and leased it back under a synthetic lease arrangement for a period of five years. The lease has been accounted for as an operating lease.

In October 2009, the Company entered into two sale-leaseback arrangements. Under the two arrangements, the Company sold certain manufacturing equipment for \$1,627,000 and \$1,648,000, and leased it back under a synthetic lease arrangement for a period of four years with an option to extend the lease for another 24 months. Both of the leases have been accounted for as operating leases. There was no gain on the transaction.

As described in Note O, the lease on the lot on which the new production facility is located runs for a period of 40 years. Lease payments from November 2013 through October 2016 are based on the scheduled payments. Although the actual lease payments thereafter will be redetermined at the fair rental value based on the terms of the lease, for purposes of the above disclosure of minimum lease payments, these payments are assumed to remain constant at the fiscal 2016 level for the remaining 30 years of the lease.

NOTE N – EARNINGS PER SHARE

The following table is a reconciliation of the numerators and denominators of the basic and diluted per share computations for each of the years ended October 31,:

	<u>2009</u>	<u>2008</u>
Numerator		
Net income	<u>\$ 5,638,771</u>	<u>\$ 4,379,666</u>
Denominator		
Weighted-average shares outstanding, excluding unvested restricted stock	2,445,856	2,200,753
Effect of dilutive restricted stock	<u>65,869</u>	<u>122,445</u>
Denominator for diluted earnings per share	<u>2,511,725</u>	<u>2,323,198</u>
Basic earnings per share	\$2.31	\$1.99
Diluted earnings per share	\$2.24	\$1.89

NOTE O – RELATED PARTY TRANSACTIONS

The Company leases its production and office facilities from a company that is owned by the Company's chief executive officer, its former president, two directors, and another shareholder of the Company. The lease was renewed in June 2008 with a term of 15 years and currently provides for a base rent of \$20,600

YOCREAM INTERNATIONAL, INC.

NOTES TO FINANCIAL STATEMENTS

per month for the period from July 2009 to June 2010. The lease payments increase three percent per year over the term of the lease.

In October 2006, to facilitate the bond financing, the Company entered into a new agreement to lease the adjoining warehouse facility from the same company described above. The lease has a remaining term of 37 years and currently provides for a base rent of \$16,715 per month for the period from November 2009 to October 2010. Thereafter the scheduled lease payments increase approximately 2.4% annually for the next six years. At the end of each ten year period the base rent for the first year of the succeeding ten-year period shall be determined based on the then-current fair market rental rates. The annual rent for each succeeding year during each ten year period will be increased by 3% over the preceding year. The lease agreement provides for an additional security deposit of \$200,000 (see Note F).

Payments under the leases for the years ended October 31, 2009 and 2008 were approximately \$420,000 and \$376,000, respectively.

The Company has retained the services of a law firm in which a director of the Company is a shareholder. The law firm has served as the Company's general counsel and for the years ended October 31, 2009 and 2008 billed the Company fees of approximately \$143,000 and \$77,000, respectively.

In August 2003, the Company entered into an agreement with its former president, upon his retirement after 27 years of service. As part of this agreement the Company continues to fund a \$500,000 split dollar life insurance policy until the policy is paid in full, or the event of death. The policy has been assigned to the Company as collateral for the repayment of the premiums. In the event of the death of the former employee and his spouse, the Company would be paid the amount of its premium advances. The Company's premium advances since the inception of this policy are approximately \$159,000 and \$146,000 at October 31, 2009 and 2008, respectively, and are classified as part of Intangible and Other Long-Term Assets (see Note F).

The Company also maintains a \$500,000 split dollar life insurance policy on its chief executive officer under which the Company pays the premiums. The policy is assigned to the Company as collateral for the repayment of the premiums. In the event of the death of the employee, the Company would be paid the amount of its premium advances. Since the inception of this policy such advances are approximately \$193,000 and \$178,000 at October 31, 2009 and 2008, respectively, and are classified as part of Intangible and Other Long-Term Assets (see Note F).

NOTE P – SUBSEQUENT EVENTS

In November 2009, the Company declared a special one-time dividend of \$2 per share paid on December 1, 2009 to shareholders of record as of the close of business on November 17, 2009. Total dividends paid approximate \$5,216,000.

The date to which events occurring after October 31, 2009, the date of the most recent balance sheet, have been evaluated for possible adjustment to the financial statements or disclosure was January 29, 2010, which is the date on which the financial statements were available to be issued.

Shareholder Information

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YoCream International, Inc. stock is publicly traded on the Pink Sheets
www.pinksheets.com YOCCM

Market Makers

Arnhold and S. Bleichroeder, Inc

Domestic Securities, Inc.

McAdams Wright Ragen, Inc.

Knight Equity Markets LP

Independent Certified Public Accountants
Mack, Roberts & Co., LLC
111 SW Columbia St., Suite 700
Portland, Oregon 97201

Annual Report
This report is available to shareholders of record
upon written request to :
Terry Lusetti, Director of Investor Relations

Directors & Officers

<u>Name</u>	<u>Age</u>	<u>Position held with Company and Principal Occupation During the Past Five years</u>	<u>Director Since</u>
John N. Hanna	69	Director; Chairman; Chief Executive Officer	1977
James S. Hanna	76	Director; Secretary	1977
William J. Rush	75	Director; Partner in Rush Hannula, Harkins, & Kyle, LLP Attorneys at Law	1987
Carl G. Behnke	64	Director; President R.E.B. Enterprises; Chairman of Sur La Table	1994
Joseph J. Hanna Jr.	71	Director; President of Hanna Strader PC Tax Attorney	2001
Fred M. Kinyon	71	Director; Owner of Capital Values Northwest	2004
W. Douglas Caudell	66	Chief Financial Officer	NA
Matthew Hanna	45	Asst Secretary; Senior Administrative Director	NA